MINUTES OF THE MONETARY POLICY DECISION MAKING MEETING HELD ON 10 APRIL 2013

During the meeting, members of the Monetary Policy Council discussed the current and future monetary policy decisions against the background of macroeconomic developments in Poland and abroad.

While addressing the external conditions it was pointed out that in 2013 Q1 the euro area had probably remained in recession and the outlook for recovery in this economy continued to be highly uncertain. In this context, Council members emphasised that in the recent period GDP forecasts for the euro area in 2013 had been revised downward, and economic indicators, after a certain improvement at the beginning of the year, deteriorated. Against this background attention was also drawn to weak business climate indicators in France. Yet, it was argued that in Germany, Poland's main trading partner, business conditions in 2013 Q1 were better than in the entire euro area. Moreover, it was indicated that Germany was expected to see a certain acceleration in economic activity growth in 2013 and 2014, which might be related to rising domestic demand supported by high employment and low unemployment. Attention was also drawn to a relatively favourable outlook for demand in the United States and in Japan. Yet, concerns were expressed that economic growth in some advanced economies in the subsequent years would remain relatively low – in the opinion of a few Council members also due to large share of government expenditure in GDP.

The Council members emphasised that strongly expansionary monetary policy pursued by major central banks, including the announcement of considerable quantitative easing by the Bank of Japan, might lead to intensified inflow of portfolio capital to the emerging economies, including Poland. As a result, those factors support Treasury bonds price increases, yet, in the longer term, might increase volatility of those prices and of the zloty exchange rate, in particular amidst sudden shift in risk aversion in the global markets. Yet, a few Council members remarked that the inflow of portfolio capital observed in the recent period had not been accompanied by any significant appreciation of the zloty. In turn, other Council members pointed out that recurring intensification of banking sector problems in some euro area economies might be a risk factor for Poland's financial sector.

While discussing the economic developments in Poland, Council members indicated that in 2013 Q1 economic activity had remained weak without signs of recovery. In this context, it was emphasised that industrial output in February had declined following its merely slight increase in January, whereas construction output growth continued to be negative. The Council members also pointed out that consumer demand had remained low, despite a certain improvement in consumer sentiment observed in the recent period, which was reflected in negative annual growth in retail sales in February 2013. According to the Council members, weak economic activity in Poland in 2013 Q1 was also suggested by weak business climate indicators, despite a certain improvement in some of those indicators in the recent period. Attention was also drawn to financial results of corporations which had deteriorated in 2012 Q4. At the same time, it was emphasised that financial condition of corporations exporting their output continued to be better than that of companies selling their goods in the domestic market.

While analysing the situation in the labour market, lack of wage pressure was emphasised. Acceleration in annual growth in enterprise sector wages observed in February was probably driven by the statistical base effect and was one-off in nature. Some Council members observed that low demand in the economy contributed to a further rise in the unemployment rate, which, in their opinion, might have an adverse effect on human capital, and, consequently, the economy's potential product. Yet, a few Council members expressed an opinion that the observed rise in the unemployment rate was largely the result of growing labour supply and adjustments in employment in enterprises, following the previously observed excessive employment growth. Those members argued that the labour market situation should improve with a rebound in production. The Council members also pointed to the structural features of the labour market, including its elasticity as regards employment contracts. A few of them argued that this elasticity favoured low labour remuneration which, on the one hand, helped enterprises to maintain their competitive advantage, but, on the other hand, had a negative impact on household savings and consumption. Yet, other Council members emphasised that weak geographical mobility of working population, resulting from poorly developed home rental market, was a considerable problem affecting the labour market.

Members of the Council emphasised that weak economic activity was accompanied by a decline in corporate lending growth both as regards current and investment loans and a low growth in lending to households. A few Council members also pointed to falling value of new household deposits in February. Other Council members indicated, however, that despite interest rate decrease in the recent period – the annual growth in household deposits observed in February exceeded the January growth.

While assessing the outlook for demand growth in Poland, the majority of the Council members believed that in the coming quarters GDP growth should accelerate, albeit would remain moderate. Slightly higher GDP growth would be, in the opinion of some Council members, the result of somewhat accelerating export growth driven by improving conditions in the German economy in the subsequent quarters. A few Council members also pointed out that declining inflation would stimulate purchasing power of consumer income which would, in turn, support domestic demand. Yet, some Council members were of the opinion that recovery in the Polish economy might be delayed, and the moment and scale of GDP growth acceleration were subject to uncertainty, especially given the uncertainty about recovery in the euro area. Other Council members, however, argued that GDP growth acceleration in the subsequent quarters might be stronger than indicated by the March projection of the NBP.

With reference to inflationary processes, Council members highlighted the fact that the CPI index had decreased below the lower limit for deviations from the target – as well as the level envisaged in the March projection. In this context they pointed to a decline in all core inflation measures, confirming low demand pressure prevailing in the economy. Yet, a few Council members were of the opinion that the recently observed decline in inflation had largely been the result of supply shocks. Most Council members believed that CPI inflation would continue to run below the lower limit for deviations from the NBP inflation target, whereas core inflation would remain low and stable. However, some Council members pointed to factors that might drive future inflation higher than forecasted. It was pointed out that amidst low tax revenues, there was a significant likelihood of the VAT rate being kept at the elevated level into 2014, which would shift up the CPI inflation path for 2014 indicated by the March NBP projection. Yet, other Council members argued that higher-than-assumed VAT rate would curtail the purchasing power of households' income, thus limiting demand pressures in the economy. In addition, some Council members indicated short-term upward risks to prices, relating to the prolonged winter, which could contribute to increase in the prices of food and municipal services. A few Council members also observed that the current and forecast core inflation was running at levels which in the past had allowed to keep CPI inflation within the symmetrical tolerance band of deviations from the target.

While discussing the level of the NBP interest rates it was agreed that these should be kept unchanged at the present meeting, in particular amidst ambiguous signs of a possible economic recovery in the subsequent quarters. At the same time, while addressing future decisions, some Council members were of the opinion that another interest rate cut in the coming months might be justified should there be no clear signs of rebound in the Polish economy, and should the likelihood of inflation persisting below the NBP target in the medium term rise. In the opinion of these Council members, an argument in favour of a further rate cut would be that real interest rates remained relatively high due to sharper than forecast inflation decline combined with decreasing inflation expectations, and the absence of clear signs of recovery in the Polish economy. At the same time, some Council members emphasised the fact that the relatively large interest rate disparity vis-a-vis advanced economies might fuel the inflow of portfolio capital to Poland, particularly in the environment of high liquidity in the global markets which received an additional boost from a marked increase in monetary expansion by the Bank of Japan.

Some Council members believed, however, that the NBP interest rates should not be lowered further, as GDP growth was anticipated to accelerate in the subsequent quarters and CPI inflation in 2014 was likely to run above the level envisaged by the projection. A few of those Council members argued that further interest rate cuts might limit the scale of restructuring of unprofitable enterprises, hampering reallocation of resources towards more productive enterprises. At the same time, in their opinion, further NBP interest rate cuts would not support demand in the economy, as the current downturn was mainly caused by weak sentiment of economic agents and low external demand growth. These members also believed that interest rate cuts might lead to an excessive rise in Treasury bond prices, which could increase the macroeconomic risk in the event of a sudden outflow of capital in the future. Other Council members argued that keeping real interest rates at a relatively high level would stimulate deposit growth, thus supporting the stability of the banking sector, in particular amidst the uncertainty about the stability of the banking sector persisting in some euro area countries.

The Council decided to keep the basic interest rates unchanged at the following levels: reference rate at 3.25%, lombard rate at 4.75%, deposit rate at 1.75%, rediscount rate at 3.50%.

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